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May 9, 2005

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Federal Communications Commission
Office of Secretary

*By Hand Delivery*

Ms. Marlene H. Dortch
Secretary
Federal Communications Commission
445 12th St, S.W., TW-B204
Washington, D.C. 20554

**Re: WC Docket No. 05-75 – In the Matter of Verizon Communications Inc. and MCI, Inc. Applications for Approval of Transfer of Control**

Dear Ms. Dortch:

Qwest Communications International Inc. ("Qwest"), by its attorneys and pursuant to the Commission's *Public Notice* (DA 05-762) and *Order Adopting Protective Order* (DA 05-647) in the above-referenced proceeding, submits herewith (1) the original of its unredacted, confidential comments, and (2) the original and one copy of its redacted, public comments in connection with the proposed merger of Verizon Communications Inc. and MCI, Inc.

Pursuant to the Commission's *Order Adopting Protective Order*, Qwest separately is submitting two copies of its unredacted, confidential comments to Gary Remondino of the FCC's Wireline Competition Bureau's Policy Division.

Each page of Qwest's confidential submission is appropriately stamped pursuant to the *Order Adopting Protective Order*. Inquiries regarding access to Qwest's confidential submission (subject to the terms of the Protective Order) should be addressed to the following:

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Please contact the undersigned if you have any questions concerning this submission.

Respectfully submitted,

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**Before the**
**FEDERAL COMMUNICATIONS COMMISSION**
**Washington, D.C. 20554**



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| Verizon Communications Inc. and | ) | |
| MCI, Inc. | ) | WC Docket No. 05-75 |
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| Transfer of Control | ) | |

# PETITION TO DENY OF QWEST COMMUNICATIONS INTERNATIONAL INC.

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May 9, 2005

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## PETITION TO DENY OF QWEST COMMUNICATIONS INTERNATIONAL INC.

Qwest Communications International Inc. ("Qwest") submits this petition to deny the application of Verizon Communications Inc. ("Verizon") and MCI, Inc. ("MCI"), for approval of their proposed merger (the "Merger Application" or "Application"). 1/ For the reasons explained below, this application should be denied in its current form.

## I. INTRODUCTION AND SUMMARY

### A. The Commission Should Reject Verizon's Theme that Re-Concentration is "Inevitable," and Address the Transparent Harm to Wholesale and Retail Competition

Qwest has a direct interest in this matter, which leads it to take the extraordinary step of opposing another RBOC's transaction. We are the only RBOC that has competed seriously outside our region. We would be directly harmed by the elimination of MCI as a provider of wholesale access in the Verizon region. After the merger, MCI no longer will act as an independent source of wholesale supply, or as a restraint on Verizon's access pricing.

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1/ *FCC Public Notice*, "Commission Seeks Comment on Applications for Consent to Transfer of Control Filed By Verizon Communications Inc. and MCI, Inc.," DA 05-762 (rel. March 24, 2005).

Furthermore, this merger must be viewed in the context of SBC's pending attempt to buy AT&T. 2/ Barely two weeks after that deal was announced, the proverbial "other shoe" dropped and Verizon entered into a parallel agreement to acquire MCI. Like SBC – Verizon is proposing to foreclose competition by acquiring one of its two primary rivals in the wholesale and retail markets in its large 29 state local service territory. 3/ Like SBC capturing AT&T – Verizon is trying to eliminate MCI as a competitive threat in its region before MCI can partner with others, including emerging cable, wireless, and VoIP providers. Verizon is thus trying to increase barriers to actual and potential competition in its region now – before it is too late.

Together, these two mergers present perhaps the most significant issues that the Commission has faced since Divestiture. The nation's two largest local exchange carriers, who already control the nation's two largest wireless companies, now propose to acquire their two largest competitors in the wireline local and interexchange markets. If the mergers are allowed, these two giants would control 80% of the nation's wireline business market, more than 63% of all ILEC lines, and more than half of all wireless subscribers nationwide. 4/ They would eliminate the two primary independent wholesale local networks in the country. Ordinarily, mergers resulting in such concentration levels would be rejected out of hand under standard Merger Guidelines analysis.

Indeed, the anticompetitive effects of each individual merger are multiplied by the way they intersect. First, and most obviously, SBC and Verizon are helping each other by eliminating

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2/ Declaration of B. Douglas Bernheim (May 9, 2005) ("Bernheim Declaration") at ¶¶ 33-34.

3/ *Id.* at ¶ 11.

4/ *See FCC Statistics of Communications Common Carriers, 2003/2004 Edition,* released Oct. 12, 2004, Table 2.1 (Total Access Lines); UBS Wireline Telecom Play Book, January 14, 2004, and company SEC filings; Deutsche Bank Data Book, Volume 8, March 2005 at 2.

the two companies that have presented the most significant competition to both of them – including competition in wholesale services used by other smaller firms. And second, SBC and Verizon have a demonstrated history of limiting their entry into each other's regions. If these mergers are approved, there is every reason to conclude that this mutual forbearance would continue. Post-merger, SBC and Verizon may compete for the largest national accounts, and in certain selected markets. They presumably would not simply dump out-of-region customers they initially inherit from AT&T and MCI. But neither RBOC can be expected to compete with the other as actively and aggressively as AT&T and MCI do today, especially with respect to customers primarily located in the other giant's service territory. Verizon and SBC have not done so before, even when it would have been easy to cross the border into each other's territory in Connecticut, or New York, or Southern California, or Texas, or many other parts of the country. They have declined to compete even when this Commission ordered them to do so as a condition to prior mergers.

Why would the de facto détente of SBC and Verizon suddenly end now? And in particular, why would they aggressively overbuild each other's local networks, check each other's wholesale pricing, and provide alternative supply to third party competitors? The answer, of course, is that they will not do so.

In short, if these mergers are approved, the result would be two large regional giants, less competitive choice for retail customers, and fewer wholesale alternatives and higher input prices for carriers hoping to compete in the two-thirds of the country controlled by these two companies.

Qwest recently has asked the Commission to reject re-concentration and reject the SBC-AT&T merger. 5/ Verizon's application here is largely – and not surprisingly – an echo of the one filed by SBC. Like SBC, Verizon promotes a theme that the two mergers are simply inevitable, and therefore implies that they should be reviewed quickly and without detailed scrutiny. Like SBC, Verizon withholds or blurs key facts concerning the scope of the overlap that would be created by these mergers. Like SBC, Verizon ignores the adverse impact of the mergers on developing intermodal competition, even while dismissing the relevance of its control of one of the nation's two largest wireless firms.

Qwest strongly rejects the notion that mergers involving such remarkable concentration and harm to competition are "inevitable," let alone in the public interest. Qwest has a much different vision. We believe that consumers are better served by application of standard competition analysis and rejection of these mergers. Importantly, we are not suggesting that AT&T and MCI will continue as they are today. All companies in this dynamic industry are evolving. But rejection of these two mergers would leave AT&T and MCI free to partner with other firms that are bringing new competition to SBC and Verizon through the possibilities of the Internet, convergence of technology and media platforms, and many other recent advances.

To be clear, our position has nothing to do with our prior bid to acquire MCI. We regret that the MCI Board rejected our higher offer, but that matter is of no concern to this Commission. We remain committed to the goal of competing with Verizon and SBC in their regions.

But these two mergers would make such competition far more difficult, for Qwest and for others. MCI and AT&T play a crucial role as providers of wholesale services bypassing Verizon and SBC (and thereby act as key competitive constraints on their wholesale prices). They also

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5/ *Petition to Deny of Qwest Communications International Inc.*, WC Docket No. 05-65 (filed Apr. 25, 2005) ("*Qwest SBC-AT&T Petition*").

are the parties best positioned, by their size and scope, to build alternative access facilities in the future, to purchase Verizon and SBC access in volume and resell to others, and to act as the bellwethers in negotiating and arbitrating interconnection agreements with those RBOCs. MCI and AT&T also are the most likely potential partners to emerging companies who would compete with Verizon and SBC in the future. These partners may be wireline companies, wireless companies, ISPs, cable companies, or some combination. Media companies also may have a role. While a Qwest-MCI combination would have been one way to enhance competition with Verizon and SBC, there are many other possibilities. It is not the Commission's job to decide which of these pro-competitive outcomes might be best. But the Commission is responsible for ensuring that Verizon and SBC do not destroy competition by capturing MCI and AT&T for themselves.

If AT&T had not offered itself up to SBC, it would be the loudest opponent of the Verizon-MCI merger. The converse also is true; MCI would be the most vigorous critic of the SBC-AT&T combination. These two transactions completely fail the Communications Act's mandate that a merger must be shown to "enhance competition" – defects that AT&T and MCI have not hesitated to address in transactions with far less competitive harm.

Indeed, it is hard to imagine a comparable situation, where the two most dominant firms in an industry "silence by acquisition" their next largest competitors, and do so at the same time. This places a particular burden on the Commission to protect the public interest by carefully investigating the facts. Verizon and SBC purport to wrap themselves in self-serving cloaks of "inevitability." It is up to the Commission to stand up and make clear that these two emperors have no clothes.

### B. If the Merger is Not Rejected, it Should be Conditioned on Broad In-Region Divestiture and Meaningful Conditions

If the Verizon-MCI merger is not rejected, the Commission at least must take steps to address the primary competitive harms that this re-concentration would cause. First, any approval would have to be conditioned on substantial divestiture of MCI facilities, customer contracts, and related operations in the Verizon territory. The Department of Justice ("DOJ") was prepared to require such divestitures of Qwest just 15 months ago when the company proposed to acquire Allegiance Telecom, a national CLEC overlapping Qwest only in its five largest and most competitive in-region cities. The Department took this position after six weeks of detailed analysis of these few markets.

We have previously discussed the DOJ consent decree in the context of the SBC-AT&T deal, a merger that is a "Super-Super-Sized" version of the Qwest-Allegiance transaction. 6/ Verizon-MCI is "Super-Super-Sized Part II." It similarly involves (i) two much larger companies than Qwest and Allegiance, and (ii) far more service overlap across the entire RBOC region, with (iii) added competitive issues arising from Verizon's ownership of Verizon Wireless Corporation ("Verizon Wireless"). Prior to ending its bid for MCI, Qwest made clear that it was prepared to make appropriate in-region divestitures of MCI customers and facilities in its region. Given the far greater harm that would arise from a Verizon-MCI merger, substantial divestures of in-region MCI operations and customers are critical – on the same terms that DOJ was requiring of Qwest just a year ago.

But divestiture alone is not enough to make up for the loss of competition from elimination of MCI, especially when coupled with the loss of AT&T, and the predictable

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6/ *Id.* at Section VII.

forbearance by SBC and Verizon from competing aggressively in each other's markets, especially in wholesale markets. The Commission also must impose conditions on Verizon and SBC wholesale services to ensure that Qwest and other competitors can compete in those two regions even after the proposed reconcentration goes forward. Again, the better decision is to deny the two mergers outright. But absent that, ground must be laid for replacement of the competition that immediately would be lost.

## II. VERIZON MUST DEMONSTRATE THAT ELIMINATION OF ONE OF ITS TWO PRIMARY RIVALS SOMEHOW "ENHANCES COMPETITION"

The Commission has clearly articulated the burden of proof on applicants for authority to merge. Under Sections 214(a) and 310(d) of the Act, "[a]pplicants bear the burden of demonstrating that the proposed transaction is in the public interest," taking into consideration the "broad aims of the Communications Act." 7/ This examination "necessarily subsumes and extends beyond the traditional parameters of review under the antitrust laws." 8/

> In order to find that a merger is in the public interest, we must, for example, be convinced that it will enhance competition. A merger will be pro-competitive if the harms to competition – *i.e.*, enhancing market power, slowing the decline of market power, or impairing this Commission's ability properly to establish and enforce those rules necessary to establish and maintain the competition that will be a prerequisite to deregulation – are outweighed by benefits that enhance competition. If applicants cannot carry this burden, the applications must be denied. 9/

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7/ *Applications of NYNEX Corporation, Transferor, and Bell Atlantic Corporation, Transferee, For Consent to Transfer Control of NYNEX Corporation and Its Subsidiaries*, File No. NSD-L-96-10, *Memorandum Opinion and Order*, 12 FCC Rcd 19985, 20007 (¶ 29) (rel. Aug. 14, 1997) ("*Bell Atlantic-NYNEX Merger Order*").

8/ *Id.* at ¶ 2.

9/ *Id.* (emphasis added).

AT&T presumably will not be commenting here on the proposed Verizon-MCI merger, but it already spoke cogently on the subject when Verizon (then Bell Atlantic) proposed to acquire GTE: "It is virtually always more profitable for rivals to merge than compete. Where such profitability comes at the expense of competition, however, consumers are harmed." 10/ AT&T discussed how that transaction "would cause substantial harm to local competition within their in-region markets by eliminating the other Applicant as a potential competitor." 11/ AT&T expressed these same concerns in the context of SBC's acquisition of Ameritech. 12/

Ultimately the Commission approved the Bell Atlantic-GTE and SBC-Ameritech mergers, but not without extended consideration of the potential competition issue, and merger conditions requiring Bell Atlantic and SBC to compete outside their respective service territories. 13/ As the Commission knows, those conditions largely failed.

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10/ *In the Matter of GTE Corp., Transferor, and Bell Atlantic Corp., Transferee, For Consent to Transfer of Control*, CC Docket No. 98-184, *Affidavit of John W. Mayo and David L. Kaserman on Behalf of AT&T Corp.* at ¶ 60 (emphasis added).

11/ *In the Matter of GTE Corp., Transferor, and Bell Atlantic Corp., Transferee, For Consent to Transfer of Control*, CC Docket No. 98-184, *Opposition of AT&T Corp. to Applicant's Supplemental Filing and Renewal of AT&T's Petition to Deny*, Mar. 1, 2000, at 6.

12/ AT&T warned that: "By combining and shielding their monopoly markets from the most powerful, imminent source of competition – each other – Applicants can continue to foreclose the development of local competition by others and further entrench their monopoly power." *In the Matter of Applications for Consent to the Transfer of Control of Licenses and Section 215 Authorizations from Ameritech Corp., Transferor, to SBC Communications Inc., Transferee*, CC Docket No. 98-141, *Petition of AT&T Corp. to Deny Applications*, Oct. 15, 1998, at i-ii; *see also id.* at 6-9.

13/ *In the Matter of GTE Corp., Transferor, and Bell Atlantic Corp., Transferee, For Consent to Transfer Control*, CC Docket No. *98-184, Memorandum Opinion and Order,* 15 FCC Rcd 14032, 14182-84 (¶¶ 319-323) (2000) *("GTE-Bell Atlantic Merger Order")*; *In the Matter of Applications for Consent to the Transfer of Control of Licenses and Section 215 Authorizations from Ameritech Corp., Transferor, to SBC Communications Inc., Transferee*, CC Docket No. 98-141, *Memorandum Opinion and Order*, 14 FCC Rcd 14712, 14877-78 (¶¶ 398-399) (1999) (*"SBC-Ameritech Merger Order").*

If AT&T had not already sold itself to SBC, it undoubtedly would speak even more forcefully here against the anticompetitive effects of the Verizon-MCI transaction. MCI is proposing a merger in which it would give up actual competition in its role as one of Verizon's two principal rivals in the Verizon service territory, and not just the potential for competition AT&T discussed in the prior mergers. As Qwest will discuss below, the harm to competition could not be more clear – as AT&T presumably would agree if it were not a party to a proposed merger itself.

## III. THE REMARKABLE MARKET CONCENTRATION IN THE VERIZON SERVICE TERRITORY WOULD BE RIVALED ONLY BY THE CONCENTRATION CREATED BY THE SBC-AT&T MERGER

### A. Verizon Has Not Provided The Data Needed To Conduct Meaningful Merger Review

As with SBC's proposed acquisition of AT&T, 14/ the most obvious competitive issue created by Verizon's proposed acquisition of MCI is the horizontal overlap between MCI facilities and services in the 29-state and the District of Columbia Verizon local exchange territory. This crucial issue arises in the context of both wholesale and retail markets.

Unfortunately, however, the two applicants have prevented the Commission and third parties from fully evaluating the scope of that overlap. They have provided little information regarding exactly where MCI operates facilities in the Verizon region, how MCI's products overlap with those of Verizon, or how many customers they each have in particular markets by service. What little data they have provided is almost entirely superficial and useless to evaluate the actual state of competition between the two companies in the Verizon region.

14/ *See Qwest SBC-AT&T Petition* at Section III.

The failure of Verizon and MCI to provide any meaningful information and data might be justifiable if the parties were proposing to eliminate all in-region overlap by divestiture. However, from the outset they have made clear that they have no such plans. Thus, for example, in testimony before the U.S. Congress on March 2, 2005, Verizon's Chairman and Chief Executive Officer asserted that there is no need to divest anything: "We don't think this transaction will cause the need to divest things the way we see it . . . ." 15/ Consistent with that position, the application here makes no mention of divestiture whatsoever.

By failing to provide adequate data regarding overlapping services and facilities in specific markets, Verizon has completely failed to meet its burden under Section 214 of the Communications Act. It has failed to make the requisite showing with regard to both wholesale and retail services.

Verizon at least concedes that there is substantial overlap between Verizon and MCI in "Verizon's region." 16/ That is a contrast to SBC, which provided virtually no data whatsoever. However, it is not always evident whether Verizon actually has supplied data for all exchange areas where Verizon offers service (in 29 states and the District of Columbia), or whether the

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15/ Testimony of Ivan Seidenberg, Hearings before House Energy and Commerce Committee at 84 (March 2, 2005). In an investor conference call soon after announcing Verizon's acquisition of MCI, Mr. Seidenberg responded to the question of whether he believed any divestitures would be necessary: "I don't think we are going to have to do any of those. There is nothing I know of that we discussed in the time – and Michael [Cappellas, President and CEO of MCI], we haven't discussed anything that we think the lawyers have said would be an issue." Ivan Seidenberg, remarks during a conference call titled *Verizon to Acquire MCI for $5.3 Billion in Equity and Cash* (February 14, 2005) (transcript available at http://investor.vzmultimedia.com/sec/sec_frame.aspx?fid=3475826).

16/ *E.g.*, Application, *Declaration of Jonathan P. Powell and Stephen M. Owens, ("Powell/Owens Declaration")* at ¶ 11 (one-third of MCI's on-net fiber locations are in Verizon's central offices); Application, *Declaration of Gustavo E. Bamberger, Dennis W. Carlton, and Allan L. Shampine ("Bamberger, Carlton, Shampine Declaration")* at ¶ 19 (MCI has fiber in **[redacted]** Verizon wire centers).

data provided are limited to the traditional Bell Atlantic service area in 13 Mid-Atlantic and Northeastern states. 17/

In any event, a close reading shows that Verizon actually has failed to provide sufficient data for a meaningful analysis of competitive issues under the standards applicable in a merger review context. 18/ A few examples demonstrate the problem:

- Verizon states that it has identified an unspecified number of "geographic areas" (a term that is not defined) where MCI has deployed local fiber facilities, and that all of such facilities in Verizon's "service territory" (again, an important term that is not defined – *see* note 17 below), are in urban or suburban areas with large concentrations of business customers. 19/ But there is no identification of the specific urban or suburban overlap areas, which clearly would be necessary to evaluate the competitive issues in those areas.

- Verizon claims to have identified 39 "areas" (again undefined) in which MCI has overlapping fiber network facilities, but again these locations are not identified. 20/

    - For each of these "areas," Verizon claims to have identified "the presence of other competitive local fiber facilities in these *collections of wire centers*," 21/ but the nature of those supposedly competitive facilities is not specified.

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17/ Professor Carlton states at least twice that his analysis is "based on nine MSAs in the former Bell Atlantic's 13-state region in which MCI operates local facilities." *Bamberger, Carlton, Shampine Declaration* at ¶ 28, n. 65 and ¶ 36, n. 81. Clearly, data is required for the all exchange areas where Verizon offers service, not merely for the 13-state former Bell Atlantic area.

18/ The Verizon data presentation also is inconsistent with MCI's prior arguments that market effects must be evaluated on a much smaller geographic basis, at the wire center or even the building level. *See, e.g., In the Matter of Unbundled Access to Network Elements,* WC Docket No. 04-313, *MCI Comments,* Oct. 4, 2004, at 28 ("[t]he relevant geographic market is the wire center"), 35. *See also In the Matter of Unbundled Access to Network Elements,* WC Docket No. 04-313, *Comments of AT&T Corp.*, Oct. 4, 2004, at 15 (stating that "route-by-route analysis is the economically correct way to proceed").

19/ Application, *Public Interest Statement* (*"Public Interest Statement"*) at 31.

20/ *Id.*

21/ *Id.*

- Verizon then states that in these 39 unspecified "areas," there are a total of 92 competitive providers—none of which providers or areas are identified — and that in 92% of these "areas" (again not identified) there are two or more unidentified competing fiber providers. 22/ Again, this is an effort to portray the illusion of competition rather than provide the specific data needed under the Merger Guidelines.

- In Boston and New York, there are supposedly more than 30 competing fiber networks in the undefined "area" where MCI has deployed its fiber, but neither the "area" nor the rivals have been identified. 23/ The size of the "area" and the logic for the chosen demarcations cannot be discerned from the data provided.

- At one point, Verizon goes so far as to claim that 89% of Verizon's wire centers have "at least one" other rival, with an "*average*" of "*nearly* six per wire center" and "*in some cases as many as* 20." 24/ Clearly the use of aggregate and average data is intended to create an impression of competition across an entire area without actually providing the specific data that is required for merger review purposes.

- Verizon claims that 96% of the Verizon wire centers where MCI is collocated have at least one competitive provider with fiber facilities. Again, the competitors remain unidentified – even in the confidential wire center data provided by Verizon. 25/

- Verizon claims that 96% of the *buildings* MCI serves with on-net fiber "are located in *specific wire centers*" where "at least one" competitor has deployed fiber. But Verizon does not claim that rivals serve the same buildings that MCI serves, or even that they "could" do so. Verizon only is asserting that at least one competitor is in a wire center somewhere in the general vicinity of a building MCI serves. 26/

- In some instances, Verizon has provided only aggregate data that is absolutely meaningless.

  - For example, Professor Carlton provides only aggregate data on the "Verizon region" (defined as the 13-state former Bell Atlantic region

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22/ *Id.* at 32.

23/ *Id.*

24/ *Id.* (emphasis added).

25/ Application, *Declaration of Quinten Lew and Ronald H. Lataille*, ("*Lew/Lataille Declaration*") at ¶ 10 and Exhibit 10.

26/ *Public Interest Statement* at 33 (emphasis added).

rather than the 29-state plus the District of Columbia that Verizon really serves). 27/

- Professor Carlton then claims that "*several* [an unspecified number] CLEC providers [unidentified] will have facilities after the transaction in *nearly all metropolitan areas* in Verizon territory with a population of 500,000 where MCI operates CLEC facilities," but he does not identify either the metropolitan areas or the providers. 28/

- Professor Carlton also claims that 95% of the MSAs have three or more CLECs, but again fails to identify the area or the CLECs. 29/

- In fact, Professor Carlton concedes that he has "not analyzed the extent to which CLEC's facilities in a given MSA serve the same areas." 30/ Obviously, this is a critical concession because this is one of the essential analyses required in this docket – but Verizon's own expert concedes that he has not undertaken the necessary review.

The Commission cannot undertake its statutory obligations based on aggregate and average data such as that provided by Verizon. Instead, the Commission (and third parties) require meaningful data that allows full evaluation of the overlap between all Verizon and MCI services and facilities wherever located at a much more granular level as required by the Merger Guidelines. A data request similar to the one the Commission has sent to SBC and AT&T would be a useful start.

### B. Notwithstanding the Defects in Verizon's Application, it is Obvious that the Merger Will Dramatically Increase Concentration and Severely Harm Both Wholesale and Retail Markets

Notwithstanding the omissions in Verizon's application, it is clear that the merger would re-concentrate wholesale and retail markets far beyond the levels permitted under standard merger review. The basic parameters of the transaction are clear, and of course they raise serious

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27/ *Bamberger, Carlton, Shampine Declaration* at ¶¶ 51, 76, and Tables 1 and 2.

28/ *Id.* at ¶ 76 (emphasis added).

29/ *Id.* at ¶ 51.

30/ *Id.* at n. 64 (emphasis added).

competitive questions on their face. Verizon is the nation's largest telephone company with more than $71 billion in revenue in 2004 and more than 200,000 employees. 31/ The 29-state Verizon territory includes some of the nation's most heavily populated areas and major business centers, including New York, New Jersey, Pennsylvania, Massachusetts, Maryland, Virginia, and the District of Columbia, and major areas of California, Texas, Illinois, Wisconsin, Indiana, Michigan and Ohio. 32/ Verizon boasts on its web site that "[w]ith more than 52 million access lines in 67 of the top 100 U.S. markets, and 9 of the top 10, Verizon reaches one-third of the nation's households, more than one-third of Fortune 500 company headquarters, as well as the Federal Government." 33/

MCI is the nation's second largest competitive carrier, behind only AT&T, with over $20.7 billion in revenue in 2004, and more than 40,000 employees. 34/ MCI states that "with millions of business and residential customers, [MCI] is a leader in serving global business, government offices, and U.S. residential customers." 35/ In 2004, MCI generated $5.1 billion in revenue from its mass market customers and $4.8 billion from its enterprise customers. 36/ Today, MCI offers products and services to businesses, governments, and consumers, including bundled local and long distance service throughout the contiguous 48 states and the District of Columbia, as well as bundled residential local, long-distance, and high speed DSL service in 34

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31/ Bernheim Declaration at ¶ 16.

32/ *Id.* at ¶ 18.

33/ http://investor.vzmultimedia.com/business.

34/ Bernheim Declaration at ¶ 21.

35/ http://global.mci.com/about/company.

36/ MCI 2004 Form 10-K (March 16, 2005) at 47 and 49.

states and the District of Columbia. 37/ It goes without saying that a substantial percentage of MCI's customers are in the 29-state Verizon local service territory.

Like SBC and AT&T, Verizon and MCI attempt to divert attention from this huge overlap with the disingenuous assertion that their merger is merely the combination of "complements" rather than the elimination of competitors, and that this combination will enhance rather than reduce competition. 38/ This is simply not true. A few months prior to the merger announcement, Verizon's CEO candidly acknowledged that there is "lots of overlap" between Verizon and MCI:

> So there's lots of overlap there. So my view is we are both serving lots of overlap in the same market. We come at it from different ways. They [MCI and AT&T] will win some business; we will win some business. And I think I will leave it at that. 39/

The Commission, of course, cannot – and must not – simply "leave it at that." Comprehensive information must be required from both companies, and then analyzed by the Commission and interested parties, with respect to the extensive overlaps in key service markets and in each relevant geographic area in the Verizon local service area.

### 1. Wholesale Markets

To begin with, the merger would directly harm competition in the market for wholesale inputs required by all Verizon competitors, including new competitors appearing as convergence matures. Verizon is the primary source of unbundled network elements and collocation required

37/ *Id.* at ¶¶ 20-21.

38/ *Bamberger, Carlton, Shampine Declaration* at ¶ 7.

39/ *Ivan Seidenberg, Verizon CEO*, Goldman Sachs Research Communicacopia XIII Conference, Oct. 6, 2004 (emphasis added).

*by facilities-based CLECs in its region. 40/ It is the primary source of special access and* transport services rivals need to reach customer premises. 41/ It is the dominant provider of switched access, especially terminations to its enormous wireline PSTN customer base.

Verizon's acquisition of MCI would seriously harm competition in the wholesale market, and do so in several ways. First, and most obviously, Verizon would eliminate one of its two most significant wholesale competitors by consolidating the MCI wholesale facilities and services in its region. 42/ MCI is the nation's second largest CLEC and has deployed the most alternative local facilities across the country, including in Verizon's region. 43/ Last year MCI generated $3.1 billion in revenues from its wholesale operations. 44/ Qwest and other Verizon competitors rely on MCI facilities to bypass Verizon today. 45/ According to its Application, MCI has established a total of [**redacted**] on-net fiber-based collocations and direct on-net connections to approximately [**redacted**] customer buildings across the nation. It should come as no surprise that many of these wholesale facilities are in the Verizon region. MCI even concedes that in deciding where to build facilities, it "targeted those incumbent LEC wire centers with the highest levels of demand for communications services," many of which are in the Verizon region due to the simple fact that Verizon's region includes some of the largest business and population centers in the country. 46/ Indeed, based on the limited information already

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40/ Bernheim Declaration at ¶ 46.

41/ *Id.*

42/ *Id.* at ¶ 47.

43/ *Id.*

44/ MCI 2004 Form 10-K (March 16, 2005) at 52.

45/ *See, e.g.*, Testimony of Jeffrey Citron, CEO of Vonage Holdings Corp., and Carl Grivner, CEO of XO Communications, Inc., Before the Senate Judiciary Committee (April 19, 2005), *available at* http://judiciary.senate.gov.

46/ *Powell/Owens Declaration* at ¶ 11.

provided, it appears that MCI's fiber facilities are either collocated at or pass through a large number of Verizon wire centers, including Verizon's most profitable wire centers, and that more than one-third of MCI's direct on-net buildings are in the Verizon region. 47/ By acquiring MCI, Verizon is capturing those facilities and removing them from competition.

Second, Verizon is eliminating one of the two most likely potential wholesale competitors in geographic locations not yet served by alternative facilities. 48/ MCI has been expanding its local networks in recent years, significantly more so than any other CLEC besides AT&T. 49/ This reflects the relatively greater incentives and ability MCI has to bypass the LEC, arising from its larger customer base and associated demand and scale economies. But for this merger, MCI would continue to have the incentives and scale economies to deploy more local facilities to reduce its dependence on Verizon. MCI also would have incentives to make those alternative facilities available to other Verizon competitors.

This is not to minimize the practical constraints on wireline bypass in certain geographic markets. MCI has repeatedly argued that even a company its size is not able to justify investment in high capacity loops and transport services in many locations, and hence it is dependent on Verizon and other LECs to reach a high percentage of customer premises. 50/ But if MCI is no longer on the scene to deploy new local facilities, for itself and for other Verizon

47/ Bernheim Declaration at ¶ 56.

48/ *Id.* at ¶ 55.

49/ *Id.* at ¶ 48.

50/ *See, e.g.*, MCI Comments, *Unbundled Access to Network Elements, Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers*, WC Docket No. 04-313 & CC Docket No. 01-338 (filed Oct. 4, 2004) at 129-130. *See also AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, RM-10593 (filed Oct. 15, 2002) at 4-5.

competitors, it is certain that competition to Verizon will suffer. 51/ Verizon/MCI will control the largest share of the market, and the largest customers; their rivals will lack the scale necessary to invest in competing facilities. 52/

Third, MCI (like AT&T) plays a key role as a reseller of local access services that they purchase in volume from Verizon based on their larger scale. 53/ Few if any carriers besides MCI and AT&T can purchase access in sufficient volumes to allow them to obtain significant discounts. Verizon is eliminating one of those special access resellers here.

Fourth, MCI (along with AT&T) acts as a key bellwether in negotiating and arbitrating interconnection agreements with Verizon. MCI's and AT&T's agreements provide benchmarks for interconnection terms. Even with the elimination of "pick and choose," their agreements provide vehicles by which smaller competitors can opt into new agreements of their own without lengthy and expensive processes. Post-merger MCI no longer will play that vital role.

Finally, all of these problems are made far worse by the pending SBC/AT&T merger. 54/ AT&T is the other large region-wide CLEC in the Verizon territory. 55/ Yet, as discussed in Section VI below, SBC and Verizon are not likely to compete aggressively in one another's region, particularly in the local wholesale market.

It is relevant that Section 251(c) of the Act requires ILECs (such as Verizon) to make available UNEs at prices established pursuant to Section 252(d)(1)(A) where competitors are "impaired" under the Section 251(d)(2) standard. The clear intent of the Act was to spur the

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51/ Bernheim Declaration at ¶ 56.

52/ *Id.* at ¶¶ 48 and 57.

53/ *Id.* at ¶ 54.

54/ *Id.* at ¶ 53.

55/ *Id.* at ¶¶ 47-48.

growth of true "facilities-based" competition within local exchange markets. 56/ The existence and operation of MCI as an independent and vital competitor within Verizon's local exchange markets goes a long way toward both providing and documenting the facilities-based competition that the Act is meant to support and sustain. 57/ It also reduces the "impairment" suffered by competitors in the absence of unbundled access to Verizon's facilities. 58/ In any event, UNEs are no substitute for the real facilities-based competition that would be lost through the proposed merger.

For all of these reasons, the Commission cannot complete its review of this merger until it fully evaluates all overlap between MCI and Verizon wholesale local exchange services and facilities, as well as the likely consequences of elimination of MCI as a continuing Verizon overbuilder. 59/

Verizon's acquisition of MCI probably would give Verizon the unilateral ability to raise prices in its region. MCI may be the next-best substitute for Verizon, especially given that SBC is unlikely to use AT&T's local assets to compete aggressively with Verizon in the local wholesale market. Antitrust law recognizes that unilateral anticompetitive effect can occur when

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56/ *See In the Matter of Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, CC Docket No. 96-98, *Third Report and Order and Fourth Further Notice of Proposed Rulemaking*, ¶ 14 (rel. November 5, 1999) (noting "preference for development of facilities-based competition"); *Verizon Communications., Inc. v. FCC*, 535 U.S. 467, 122 S. Ct. 1646, 1669 (2002) (finding a Congressional intent to stimulate facilities-based competition).

57/ Bernheim Declaration at ¶ 57.

58/ By establishing a test for impairment based on the number of fiber-based collocation cages in a given wire center, the Commission expressly recognized that the absence of statutory impairment could be evaluated based on the number of independent competitors in a market. *See In the Matter of Unbundled Access to Network Elements; Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers*, WC Docket No. 04-313, CC Docket No. 01-338, *Order on Remand* at ¶ 66 (rel. Feb. 4, 2005).

59/ Bernheim Declaration at ¶ 112.

merging firms with differentiated products are close substitutes for one another. 60/ The likelihood of unilateral anticompetitive effects increases where consumers "regard the products of the merging firms as their first and second choices" and it is unlikely that remaining firms in the market will reposition their products to replace the competition lost between the merging firms. 61/ The *Merger Guidelines* presume that consumers "regard the products of the merging firms as their first and second choices" where (1) the firms' market shares reflect their relative appeal to consumers; (2) the market is highly concentrated; and (3) the "merging firms have a combined market share of at least 35%." 62/

Thus, for example, *FTC v. Swedish Match* involved the merger of the largest and third largest loose leaf chewing tobacco manufacturers. The FTC claimed that (1) many consumers considered the merging parties to be close substitutes, (2) the market was highly concentrated, and (3) the merging parties combined market share would exceed 60%. 63/ The court endorsed the FTC's view: "Swedish Match will raise prices as long as the profit gained by the higher prices of Swedish Match products in addition to the profits diverted to National's brands is greater than the profits lost through diversion to non-Swedish Match Brands." 64/

Here, the potential for unilateral anticompetitive effects is strong given that the market is highly concentrated, Verizon and MCI enjoy high market shares in the Verizon region, SBC is

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60/ United States Dep't of Justice & Federal Trade Comm'n, *Horizontal Merger Guidelines* ("*Merger Guidelines*") at § 2.2 (1992). *See* David T. Scheffman and Mary Coleman, *Quantitative Analyses of Potential Competitive Effects from A Merger*, June 9, 2003, available at *www.usdoj.gov/atr/public/workshops/docs/202661.htm. See also* Dennis W. Carlton & Jeffrey M. Perloff, *Modern Industrial Organization* (2000).

61/ *Merger Guidelines* at § 2.21.

62/ *Id.* at § 2.211.

63/ *FTC v. Swedish Match*, 131 F. Supp. 2d 151, 169 (D.D.C. 2000)

64/ *Id.* at 169-70.

unlikely to use the AT&T wholesale assets to compete aggressively in Verizon's territory, and Verizon and MCI have significant brands and customer recognition. The *Merger Guidelines* presume market power from such high concentration. The full extent of the unilateral effects problems caused by the proposed Verizon/MCI merger only will become clear after Verizon and MCI supply sufficient data to allow a meaningful analysis. But there certainly is reason for serious concern.

### 2. Retail Markets

Verizon and MCI similarly fail to provide any disaggregated data regarding competition in the retail market in the Verizon territory, even though they are the two largest service providers. 65/ The parties generally ignore the question of where and how their services overlap, and instead argue that this overlap is irrelevant given competition from other parties. 66/

Qwest agrees that competition is growing in the retail telecommunications market. However, Verizon and MCI overstate the scope of that competition in Verizon's region. They ignore the extent to which that competition depends on use of Verizon wholesale facilities discussed above, and the ability of competitors to bypass Verizon using MCI facilities. They also ignore the relevance of Verizon's own large position in the wireless market.

Because of these problems, the potential for unilateral anticompetitive effects also exists in the retail market. 67/ Even the limited data and information now available show that MCI is the next-best substitute for Verizon based on combined market shares, that the marketplace is highly concentrated, and that other firms are likely unable to replace the competition that will be lost following this merger.

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65/ Bernheim Declaration at ¶ 65.

66/ *Id.*

67/ *Id.* at ¶¶ 65-88

Verizon tries to avoid these facts by characterizing its services as complementary to MCI rather than direct substitutes. 68/ Verizon points to itself as serving local and regional business customers, while describing MCI as operating an expansive national and international wireline network, and a large Internet backbone serving large enterprises. 69/

Verizon executives sang a very different tune prior to the merger announcement. For example, Verizon's Chief Financial Officer noted last year, "[a]nother key part of our strategy is the Enterprise and Business segment. As you may have seen, a recent Yankee Group study indicated that we are the market leaders in this segment with a 22.4 percent market share." 70/

Market share data from TNS Telecoms confirms that Verizon is a serious competitor in the enterprise market segment. In New York City, for example, TNS Telecoms reports that **[redacted]** has a **[redacted]** share of enterprise local lines, followed by **[redacted]** with **[redacted ]** and **[redacted ]** with **[redacted]**. 71/ Combined, Verizon and MCI will control **[redacted ]** of the enterprise local lines. Today, Verizon and MCI receive **[redacted]** of the revenue from all enterprise lines in New York City. 72/

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68/ *Public Interest Statement* at 1.

69/ *Id.* at 13.

70/ Comments of Doreen Toben, Verizon CFO, First Quarter 2004 Earnings Conference Call, April 27, 2004. *See also* Comments of Ivan Seidenberg, Verizon Chairman and CEO, Second Quarter 2003 Earnings Conference call, July 29, 2003 ("[T]he fact is that when you look at who we signed these contracts with, they're right in the wheelhouse of the IXCs. They're all the Wall Street firms, they're all of the big automotive firms – you know, the one that have initials GM – you know, you could figure that out. You know, so I think that we are winning business in all of these accounts."); Larry Babbio, Verizon Vice Chairman, Fourth Quarter 2004 Earnings Conference Call, January 29, 2004 ("The fact is, customers . . . look at us as a very serious player in the Enterprise market") (emphasis added).

71/ *See infra,* at 23.

72/ *Id.*

The Commission, of course, knows that Verizon and MCI compete heavily against one another. Both of these companies offer full telecommunications product sets in competition with one another. In its most recent Form 10-K filed with the Securities and Exchange Commission, Verizon asserts that:

> Verizon Communications Inc. is one of the world's leading providers of communications services. Verizon's domestic wireline telecommunications business provides local telephone services, including broadband, in 29 states and Washington, D.C. and nationwide long-distance and other communications products and services. The domestic wireline consumer business generally provides local, broadband and long distance services to customers. Our domestic wireline business also provides a variety of services to other telecommunications carriers as well as large and small businesses. 73/

These products and services directly overlap with those of MCI.

In short, while the merger parties have held back data necessary to evaluate their retail overlap on a market-by-market basis, MCI obviously is one of Verizon's primary retail wireline competitors, across Verizon's entire territory and across all services. Data on retail consumer and business market shares for Verizon and MCI in Verizon's region demonstrate the substantial overlap between the merging companies for both consumer and business customers. In almost all cases, MCI is Verizon's largest competitor after AT&T. MCI's competitive significance in Verizon's region is only magnified with SBC's acquisition of AT&T, the history of mutual forbearance by Verizon and SBC towards one another, and the expectation of future forbearance so that SBC will not use AT&T's assets to compete aggressively in Verizon's territory. 74/

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73/ Verizon 2004 From 10-K (March 14, 2005) at 1.

74/ Because, as discussed in Section VI, there is strong reason to believe that SBC will not use AT&T's facilities to compete aggressively in Verizon's region, AT&T's future competitive significance must be discounted. Bernheim Declaration at ¶ 35.

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The parties' calculated failure to provide sufficiently detailed information regarding the scope of that overlap in the Verizon region is a prima facie failure to meet their burden of proof under Sections 214(a) and 310(d).

Finally, the parties completely fail to address the significance of Verizon's ownership of Verizon Wireless, the nation's second largest wireless company, serving 45.5 million customers, covering 90% of the U.S. population across the country, with a particularly strong presence in the Verizon region. 75/ This too is a material omission warranting rejection of the Application, especially given the parties' contention elsewhere that wireless services are a competitive substitute for the Verizon and MCI wireline services that would be consolidated by the merger.

75/ Bernheim Declaration at ¶ 87.

Under Section 1.5 of the *Merger Guidelines*, mergers of competing firms with substantial combined market shares in highly concentrated markets are presumed to create or enhance market power or facilitate its exercise in violation of Section 7 of the Clayton Act. 76/ But the Commission and third parties cannot fully evaluate the scope of the Verizon and MCI overlap here until and unless the parties themselves begin that process with reasonable granularity. Posing the same questions to Verizon and MCI that the Commission posed to SBC and AT&T would be a first step in the right direction.

In the meantime, however, Verizon and MCI bear the burden of proof regarding competition issues raised by the extent of the overlap. Absent a more comprehensive

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76/ That is why, for example, the Justice Department concluded that the Cingular/AT&T Wireless merger violated Section 7, absent remedies. As the Justice Department stated in its Competitive Impact Statement:

> "Cingular's proposed acquisition of AT&T Wireless will substantially lessen competition in mobile wireless telecommunications services and mobile wireless broadband services in the relevant geographic areas." Competitive Impact Statement, *United States v. Cingular Wireless*, Civil Action No. 1:04CV01850 (RBW) (D.D.C. Oct. 29, 2004).
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> "The individual market shares of Cingular's and AT&T Wireless's mobile wireless telecommunications services businesses in the 10 relevant geographic markets as measured in terms of subscribers range from 9 to more than 71 percent, and their combined market shares range from 61 to nearly 90 percent. In each relevant geographic market, Cingular or AT&T Wireless has the largest market share, and, in all but one, the other is the second-largest mobile wireless telecommunications services provider." *Id.* at 10-11.
>
> "Cingular and AT&T Wireless are likely closer substitutes for each other than the other mobile wireless telecommunications services providers in the relevant geographic markets." *Id.* at 11.
>
> "For these reasons, plaintiffs concluded that Cingular's proposed acquisition of AT&T Wireless will likely substantially lessen competition, in violation of Section 7 of the Clayton Act, in the provision of mobile wireless telecommunications services and mobile wireless broadband services in the relevant geographic markets." *Id.* at 13.

concentration showing that permits practical evaluation – on a service-by-service and market-by-market basis – the Application is deficient on its face and should be rejected. 77/

## IV. THE MERGER WOULD STIFLE POTENTIAL COMPETITION TO VERIZON FROM NEW TECHNOLOGIES AND CONVERGENCE

Like SBC, Verizon also attempts to discount the significance of the reconcentrating merger effects by pointing to intermodal competition from cable, VoIP, and wireless services. Qwest already has discussed the multiple defects in these arguments in connection with the SBC-AT&T merger, and we incorporate that analysis by reference here. 78/ Qwest fully agrees that the telecommunications market is in a period of change, and that competition is increasing. 79/ But the question here is how this merger, and the interrelated SBC-AT&T combination, would affect these developments. 80/

Unfortunately, Verizon gives the Commission no assistance in this analysis. Its application is full of rhetoric and statements about the potential future – virtually ignores the two-year period of review that is relevant under the Merger Guidelines. 81/ Verizon does not discuss competition and convergence in the context of particular service markets or geographic markets, or even seriously acknowledge that such analysis is necessary. Verizon ignores the Commission's recent conclusion that wireless services are not a substitute for wireline, or the

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77/ Bernheim Declaration at ¶ 112.

78/ *See Qwest SBC-AT&T Petition* at Section IV.

79/ Bernheim Declaration at ¶¶ 98-101.

80/ *Id.* at ¶¶ 102-106.

81/ *See, i.e., Public Interest Statement* at 2 ("[w]ithin five years, a fifth or more of all households are expected to give up their traditional telephones in favor of these new cable and other VoIP services") (emphasis added).

Commission's discussion of the incentives of a RBOC to manage its wireless business to minimize replacement of wireline services. 82/

Verizon also ignores the fact that intermodal competitors depend upon wholesale inputs from Verizon itself in order to provide their services. 83/ These include broadband loops to customer premises, particularly in the business market, transport, and termination services to Verizon's vast PSTN customer base. 84/ Yet this transaction would eliminate one of the two main competitors in the local wholesale market (and the other merger, followed by predictable mutual forbearance, would eliminate the other). For all of the reasons discussed above in Section III, this merger would make it harder and more expensive for competitors to access wholesale service and facilities.

Again, Qwest will not repeat here the more complete analysis of this problem that it provided in the context of the SBC-AT&T docket. Until Verizon and MCI provide actual data on actual conditions in actual product and geographic markets, this application is deficient on its face and must be rejected. 85/

## V. THE MERGER ELIMINATES A KEY "MAVERICK" IN INNOVATION

Verizon's proposed merger with MCI poses additional competition concerns because independent stand-alone providers, including MCI and AT&T, have behaved as "mavericks" in introducing innovations in telecommunications that have benefited consumers, while Verizon

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82/ *Applications of AT&T Wireless Services, Inc., and Cingular Wireless Corporation for Consent to Transfer of Control*, WT Docket No. 04-70, *Memorandum Opinion and Order*, FCC 04-255 (Oct. 26, 2004) at ¶ 247.

83/ Bernheim Declaration at ¶¶ 102-104.

84/ *Id.*

85/ *Id.* at ¶ 112.

has resisted those innovations. As a result, the proposed Verizon/MCI merger is likely to stifle important innovation that has benefited customers.

It is a well-established principle of antitrust law that the elimination of a "maverick" firm through merger or acquisition is likely to produce anticompetitive effects because of the loss of that maverick behavior. For example, Section 2.12 of the *Merger Guidelines* states:

> In some circumstances, coordinated interaction can be effectively prevented or limited by maverick firms – firms that have a greater economic incentive to deviate from the terms of coordination than do most of their rivals (*e.g.*, firms that are unusually disruptive and competitive influences in the market). Consequently, acquisition of a maverick firm is one way in which a merger may make coordinated interaction more likely, more successful, or more complete.

As one important antitrust commentator has explained, an industry maverick is a firm that is a disruptive competitive influence or that constrains more effective coordination by rivals, so removing a maverick through merger or acquisition is likely to result in higher prices. 86/ If the maverick is disruptive through innovation, then eliminating the maverick will likely reduce innovation.

MCI has played an important role in innovation in the industry, while Verizon has often balked at introducing innovations that might undermine its incumbent ILEC businesses. As a result of the proposed merger, MCI will be lost as an independent innovator.

MCI's 30 year history of introducing innovative service offerings to challenge entrenched business models and create competition is well known. That history begins, of course, with its success as the first company able to compete effectively against the dominant AT&T in long distance services. MCI's success in the long distance market was based, in large part, on its

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86/ J. Baker, *Mavericks, Mergers, and Exclusion: Proving Coordinated Competitive Effects Under the Antitrust Laws*, 77 N.Y.U.L. Rev. 135 (2002).

deployment of a technologically advanced nationwide fiber optic network and its introduction of innovative price plans, including its low-priced "5 Cents Everyday" service offering and its "Friends and Family" loyalty program. These service plans helped to reduce long distance rates throughout the 1980's and 1990's, providing immeasurable benefits for consumers. Many subsequent competitors emulated these innovative serving offerings in the long distance market, further increasing competition to AT&T. 87/

Both before and following the Telecommunications Act of 1996, MCI pioneered the development of competitive local access to bypass the ILEC local loop. To compete with Verizon and other ILECs for mass market local exchange customers, MCI launched "The Neighborhood Built by MCI" in April 2002. This innovative service offering represented the industry's truly first flat-rate, all-distance nationwide calling plan, freeing callers from the constraints of per-minute rates, time-of-day restrictions, and unnecessary boundaries between local and long distance service. Since its introduction, many competitors (both inter- and intra-modal) have imitated the flat-rate, all-distance nature of this service offering, providing enhanced competition in the local exchange services marketplace. 88/

MCI also has been an innovator in the Internet and data services market segments. Indeed, MCI was among the first carriers to recognize the transformational nature of the Internet with its introduction of "internetMCI" in the early 1990s, giving residential customers access to a portfolio of Internet-based services. As the first carrier to roll out nationwide DSL services in

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87/ *See "No-Holds-Barred Battle for Long Distance Calls," The New York Times*, January 21, 1995 (noting that Sprint introduced "Sprint Sense," a discounted long distance service plan in reaction to the success of MCI's Friends and Family program).

88/ *See In The Matter of Section 272(F)(1) Sunset of the BOC Separate Affiliates and Related Requirements and 2000 Biennial Regulatory Review Separate Affiliate Requirements of Section 64.1903 of the Commission's Rules,* FCC 03-111, 18 FCC Rcd 10914 (2003) (noting that one of the major changes in the competitive landscape has been an increase in bundled, flat-rate telecommunications service offerings).

the late 1990s, MCI was quick to realize the enormous potential in this previously-ignored technology. Finally, MCI continues to be a technological innovator in Internet backbone services. During the course of 2004, MCI achieved new levels of transmission performance when its technology trial carried 40 Gbps of traffic over a single full-duplex Optical Carrier (OC)-768 interface for the very first time. 89/

If Verizon acquires MCI, this source of innovation that has benefited consumers will instead be in the hands of a firm that has resisted innovations that might undermine its ILEC businesses. In addition, MCI is a key provider of wholesale services to other innovators, such as Vonage and XO, which have raised concerns about their ability to continue to secure those services if MCI is owned by Verizon. 90/ Verizon and MCI claim that their merger will increase innovation. But they offer no evidence for that claim, and there is substantial reason to fear that it will actually retard innovation.

## VI. THE MERGER WOULD INCREASE INCENTIVES FOR MUTUAL FORBEARANCE BY VERIZON AND SBC, ESPECIALLY IN THE WHOLESALE MARKET

Several years ago in the context of two then-pending ILEC/ILEC mergers, MCI spoke presciently about the propensities of the resulting firms to mutually forbear from competition, a phenomenon that is sure to accompany the Verizon/MCI and SBC/AT&T mergers as well. MCI said then:

> If the two pending mega-mergers were allowed to proceed, it would be easier for the remaining ILECs to reach mutually beneficial understandings to limit competition by serving out-

89/ *See "MCI Completes Year of Industry Firsts,"* MCI Press Release (December 29, 2004).

90/ *See infra,* n. 23.

> of-region locations only of customers predominantly located in their region. 91/

Qwest agrees with this pre-merger MCI position. 92/ The Commission must address the extent to which the Verizon/MCI and SBC/AT&T mergers increase the already existing incentives for those two RBOCs to refrain from aggressive competition in each other's markets. 93/ These deals present a real risk that the combined companies will engage in what economists refer to as "mutual forbearance," tacitly colluding to avoid or limit direct competition. 94/ This risk is heightened by the fact that Verizon and SBC have a history of avoiding competition with each other. 95/ Qwest believes that the two resulting merged firms' practice of détente will dramatically blunt over time what has been vigorous competition by AT&T in Verizon's region and by MCI in SBC's region. 96/

MCI correctly predicted that the SBC-Ameritech merger "alone would significantly increase the likelihood of coordinated interaction. It will make it much easier and more likely for the few remaining major ILECs to continue the non-aggression pact under which they do not compete in each other's region." 97/ AT&T has discussed this problem in even more vivid terms:

> For example, while post-merger SBC would be well poised to attack Bell Atlantic's most profitable market through its SNET territories, Bell Atlantic would likewise be well positioned to attack SBC in Los Angeles

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91/ Comments of MCI WorldCom, Inc., CC Docket No. 98-184, *In the Matter of GTE Corp., Transferor and Bell Atlantic Corp., Transferee,* Nov. 23, 1998, at 31.

92/ Bernheim Declaration at ¶¶ 33-43.

93/ *Id.* at ¶¶ 35 and 41.

94/ *Id.* at ¶¶ 34, 35, 38-41.

95/ *Id.* at ¶ 35.

96/ *Id.* at ¶ 39.

97/ *In the Matter of the Applications for Consent to the Transfer of Control of Licenses and Section 214 Authorizations from Ameritech Corp to SBC Communications Inc., Comments of MCI World Com Inc.*, CC Docket 98-141, (filed Oct. 15, 1998) at 16 (emphasis added).

> *from GTE's Orange County territory. So while SBC may have incentives* to enter the New York City metropolitan area, it knows that doing so would put its most lucrative market at risk to a significant competitor. Such "mutually assured destruction" scenarios greatly facilitate maintenance of the status quo in which both Bell Atlantic and SBC benefit by maintaining their monopolies. 98/

Importantly, at the time MCI and AT&T were focused on the loss of potential SBC/Bell Atlantic competition, and the likelihood that limited loss would promote mutual forbearance. The two mergers before the Commission today are far more dangerous in this regard because Verizon and SBC are proposing to absorb their two largest existing rivals, a blatant elimination of head-to-head rivalry that greatly worsens the harm to competition and customers attributable to the phenomenon of mutual forbearance between the two regionally powerful ILECs.

The Commission therefore should carefully investigate and, Qwest believes, conclude that these mergers will reduce competition through mutual forbearance – or "mutually assured destruction" to use AT&T's words. 99/ Verizon and SBC predictably will try to brush off this problem by mischaracterizing the point. We are not suggesting that they will never compete with one another, or that they will abandon the out-of-region customers they acquire.

The problem is more subtle and insidious, which is why it deserves such close scrutiny here. SBC and Verizon may continue to compete in the retail market for the very largest enterprise accounts, at least those that do not have disproportionate numbers of end user locations in one region or the other. But as MCI previously noted, the two parties are more likely "to reach mutually beneficial understanding to limit competition by serving out-of-region

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98/ *In the Matter of GTE Corp. Transferor, and Bell Atlantic Corp. Transferee, For Consent to Transfer of Control*, CC Docket No. 98-184, Petition of AT&T Corp. to Deny Application, (filed November 23, 1998) at 34-35 (emphasis added).

99/ Bernheim Declaration at ¶ 38.

locations only of customers predominantly located in their region." 100/ Even then, the competition may become less vigorous over time, with SBC and Verizon allocating customers between them in tacit and undetectable ways. 101/ The proposed mergers increase the incentive and ability of Verizon and SBC to use their local market power to raise entry barriers to protect their respective (now even larger) in-region business bases, while simultaneously refusing to poach from one another's territory. 102/ Each knows the source of its own and the other's market power. To maximize profitability, they will mutually avoid any ill-conceived challenge that will invite retaliation and undermine their respective strengths and reduce profitability for both firms.

This problem is likely to be the most serious in the local wholesale market. 103/ Verizon and SBC have not constructed any material local network facilities in each other's region. They will have every incentive over time to withdraw the MCI and AT&T local facilities from service, and in the interim to price them to third parties (like Qwest) at levels that do not compete with the LECs' own wholesale prices. They have no incentive to maintain or expand an overbuild of each other in the future, for such a course would place a competitive restraint on each other's local wholesale services, diminish their competitive advantages vis-à-vis others, and reduce their mutual profitability.

The Commission is familiar with the fact that Verizon and SBC have largely avoided competition, even when ordered to do so, and despite the fact that these largest RBOCs are ideally suited to compete outside of their traditional regions. Today they more than anyone else

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100/ *See infra,* at 30.

101/ Bernheim Declaration at ¶ 42.

102/ *Id.*

103/ *Id.* at ¶ 40.

have the necessary financial resources, technical expertise, and market presence to do so. The Commission has repeatedly sought to encourage ILECs to compete out-of-region for these very reasons.

Verizon and SBC presumably will respond with rhetoric and promises to compete with one another. They may present anecdotal examples of limited retail competition. The noise level is likely to increase in the months during which the mergers are pending approval.

But the past is a better guide to the future. As the Commission knows, Verizon and SBC have failed to compete with one another even when ordered to do so. 104/ When the Commission approved SBC's acquisition of Ameritech in October 1999, one of the conditions was that SBC provide local service in thirty out-of-region markets, including Boston, Miami, and Seattle, within thirty months of closing the merger. 105/ In its Order, the Commission stated quite clearly that requiring SBC/Ameritech to compete out-of-region was expected to have two crucial procompetitive effects that counter-balanced the loss of potential competition between the firms. First, SBC/Ameritech out-of-region entry was expected to provide out-of-region consumers the benefits of competition. Second, out-of-region competition was expected to encourage counter-attacking competitive entry into SBC's region by other incumbent LECs:

> This will ensure that residential consumers and business customers outside of SBC/Ameritech's territory benefit from facilities-based competitive service by a major incumbent LEC. This condition effectively requires SBC and Ameritech to redeem their promise that their merger will form the basis for a new, powerful, truly nationwide multi-purpose competitive telecommunications carrier. We also anticipate that this condition will stimulate competitive entry into the SBC/Ameritech region by the affected incumbent LECs. 106/

104/ *Id.* at ¶ 36.

105/ *SBC-Ameritech Merger Order*, 14 FCC Rcd 14712, 14826 (¶ 259) (1999).

106/ *Id.* at 14877 (¶ 398).

Less than a year later, as a condition on the acquisition of GTE, the Commission required Bell Atlantic (since renamed Verizon) to invest $500 million in out-of-region entry. 107/ Once again, the Commission noted the dual benefits to be expected from this condition:

> We believe that the Applicants' out-of-region competition commitment is sufficient to ensure that residential consumers and business customers outside of Bell Atlantic/GTE's territory will benefit from meaningful, facilities-based competitive service. We also anticipate that this condition will stimulate competitive entry into the Bell Atlantic/GTE region by the affected incumbent LECs. 108/

The Commission's Orders were largely unsuccessful because neither Verizon nor SBC has engaged in meaningful competition out-of-region. The promises Verizon and SBC made have not been kept; their out-of-region activities remain very limited. Qwest alone among incumbent LECs has competed aggressively out-of-region.

The record to date is clear: Verizon and SBC prefer an environment of détente or mutual forbearance, where neither materially encroaches on the other's territory, and they have avoided an environment of vigorous competition.

This merger, and the parallel SBC/AT&T merger, would make matters much worse. First, Verizon and SBC would be eliminating their most significant current competitors – who pose by far the greatest threat of destabilizing their existing mutual forbearance. 109/ Second, having captured the large customer base and revenue of their competitors, Verizon and SBC would have even more to protect through mutual forbearance, and even less incentive to attack one another. And third, their ability to maintain détente is strengthened by the post-merger

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107 *GTE-Bell Atlantic Merger Order* at ¶ 319.

108/ *Id.* at ¶ 321.

109/ Bernheim Declaration at ¶¶ 44-88.

symmetry of the two companies. 110/ In short, a likely outcome of the two mergers is the creation of two enormous and durable regional vertically integrated monopolies. This would not happen overnight. Rather, Verizon/MCI and SBC/AT&T would allow the existing MCI and AT&T business in each other's regions to decline through reduced competition with each other, but the likely end result is clear.

Others have commented that a combined Verizon/MCI and SBC/AT&T will result in two companies so similar to one another that mutual forbearance is a likely outcome, potentially resulting in reduced price competition. For example, a recent report by Legg Mason concluded:

> Finally, we reiterate our view that the enterprise sector is more sustainable should VZ prevail [as the acquirer of MCI] as VZ/MCI and SBC/T would have very similar business mixes and thus more aligned interests in the marketplace. Further, we note that with enterprise being one of many businesses in a portfolio, there would be less reliance on it, potentially leading to a moderation in the rate of price declines. Conversely, should Qwest win MCI, we see a maintenance of the significant pricing pressure in the enterprise arena as the combined company would still be significantly reliant on the enterprise long distance business. 111/

A "White Paper" commissioned by Verizon also similarly concluded that following these deals, Verizon and SBC will "be almost mirror images of one another with similar revenues, access lines and payrolls." 112/

That symmetry enhances the risk of tacit coordination. Symmetry, combined with each company's regional specialization, creates a mutuality of interest, as well as a mutual threat that

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110/ *Id.* at ¶ 43.

111/ Legg Mason, *Qwest Communications Int'l., Inc. NYSE: Q, Reports Indicate Continued Q/MCI Discussions*, April 19, 2005, at 1 (emphasis added).

112/ Robert A. Saunders, *Critical Implications of the Proposed Qwest MCI Merger: An Industry White Paper* (The Eastern Management Group, 2005) at 2, fn.1.

undoubtedly reduces their incentives to compete with one another. 113/ The only way Verizon and SBC can avoid the threat the other poses is to forego entry into the other's region, and thereby maintain their in-region market power. Only through this mutual forbearance can they assure themselves of their continued in-region dominance. By being nearly fully self-sufficient in their own regions, and having little relative business outside their own regions, Verizon and SBC would have no self-interest in providing non-discriminatory access to their network to others on an equal footing.

And again, the risk of mutual forbearance is greatest in the local wholesale market – the market that is most important to Qwest and other parties who seek to compete with these two giants.

The Commission should thoroughly evaluate the harm to the public that would occur if, through these mergers, Verizon and SBC create two durable, vertically integrated regional monopolies. 114/ A complete investigation of their present and planned out-of-region activities is required. At this point, it appears more likely that Verizon and SBC will reduce the vigorous competition that MCI and AT&T currently provide against the two RBOCs, rather than maintain or expand it. 115/

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113/ Bernheim Declaration at ¶ 43.

114/ *Id.* at ¶¶ 93-97.

115/ Qwest's Chairman and CEO Richard Notebaert has commented that "[t]here is nothing in these pending transactions that suggests that they will encourage either Verizon/MCI or SBC/AT&T to compete. Instead, the transactions will almost certainly reduce their need to compete by leaving them the sole contenders for long-term dominance of a market where each has substantial power." *See* Richard Notebaert, Statement and slides filed with the Securities and Exchange Commission, March 15, 2005.

# VII. THE MERGER SHOULD BE REJECTED, OR APPROVED ONLY SUBJECT TO MAJOR CONDITIONS TO ELIMINATE ALL OF ITS ANTICOMPETITIVE EFFECTS

## A. Verizon Should Have to Substantially Divest Overlapping MCI Operations in The Verizon Local Service Territory, Just as Would Have Been Required of Qwest and Allegiance a Year Ago

As Qwest considered its proposed merger with MCI, it was fully prepared to undertake appropriate divestitures of MCI assets and customers in its region. Unlike Verizon, we were not going to pretend that no divestitures would be needed.

Qwest has recent first hand experience in this area. Just over a year ago, Qwest entered into an agreement to acquire Allegiance Telecom, Inc. ("Allegiance"), a national CLEC. Allegiance operated almost entirely outside Qwest's region, and the transaction was strategically aimed at strengthening Qwest's ability to compete on a national basis. Unfortunately, Qwest was outbid at the bankruptcy court auction and was not able to close its deal.

Prior to the auction, however, Qwest engaged in six weeks of substantial discussions with the Department of Justice Antitrust Division regarding the overlap between Allegiance and Qwest's in-region business. Specifically, Allegiance served the business market in five (but only five) in-region Metropolitan Statistical Areas ("MSAs"): Denver, Minneapolis, Portland, Phoenix, and Seattle. These five MSAs are the largest in the Qwest region, and the cities where Qwest faces the most vigorous competition from AT&T, MCI, and other CLECs. Nevertheless, after very substantial discussion and investigation over at least six weeks, DOJ required that Qwest agree to divest all Allegiance business operations in the Qwest region. Specifically, shortly before the auction, DOJ and the parties agreed to a consent decree requiring the parties to agree to hold separate and divest:

- "All [Allegiance] switches, routers, transport and associated collocation facilities located in the In-Region MSAs, and all interconnection agreements used in connection with the provision of telecommunications services."

- "All [Allegiance] contracts with customers to provide telecommunications services to locations within the In-Region MSAs," as well as all related business and customer records and "business plans associated with the provision of telecommunications services to customer locations in the In-Region MSAs or with marketing to potential customers in the In-Region MSAs."

- "All [Allegiance] transport facilities physically located in whole or in part within In-Region MSAs."

- All other in-region assets of Allegiance, including real and personal property located in the In-Region MSAs, and all federal, state and local regulatory authorizations, intellectual property, all third party agreements used in connection with Allegiance service in the MSAs. 116/

DOJ allowed only three exceptions to this broad divestiture requirement for the Allegiance operations in the Qwest region.

- Primarily Out-of-Region Contracts. First, notwithstanding the general obligation to divest all in-region service to customers, Qwest was allowed to acquire specific Allegiance contracts where the majority of services were provided to the customer outside the Qwest region and it would be "impossible or impractical" to divide the revenues and responsibilities between Qwest and the third party acquiring the divested business.

- Transport between In-Region and Out-of-Region MSAs. Second, Qwest was not required to divest Allegiance interexchange transport facilities crossing its region boundaries.

- Shared Systems. Third, Qwest was not required to divest Allegiance operating and related systems used primarily to provide telecommunications outside the Qwest region that could not be divided and sold to the divestiture purchaser separately. Such systems included order entry, provisioning, billing, network monitoring and the like. However, Qwest was required to make those systems available to the buyer of the in-region Allegiance business on a transitional basis to the extent needed. 117/

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116/ Agreement among the Antitrust Division of the United States Department of Justice, Qwest and Allegiance (Feb. 11, 2004) (all citations to the Hold Separate Stipulation and Order, at Section 1(D), Definition of "Divestiture Assets").

117/ *Id.* at Sections E, F and H (definitions of "Excluded Assets," that is, in-region customer contracts, transport facilities, and shared systems excluded from general divestiture requirement).

Qwest reserved the right to continue to argue with DOJ for a less stringent divestiture after the auction and prior to closing its transaction with Allegiance. Qwest did not and does not concede that divestiture of this scope should have been required given the number of other CLECs in its five largest markets, and Qwest's own more limited market position. However, DOJ's position as of that time was clear: all of Allegiance's overlapping in-region assets had to go.

The proposed SBC/AT&T merger is essentially the Qwest/Allegiance deal "Super-Super-Sized – Part One." This deal is Part Two. MCI obviously is a far more significant competitor in the Verizon region than the bankrupt Allegiance was in only five highly competitive cities in Qwest's local territory. MCI offers many more services and facilities, and does so across all 29 states plus the District of Columbia – not merely in just a few large cites. The Verizon region is much more heavily populated, with more significant business centers and corporate headquarters. And importantly, Verizon operates a leading wireless company that coordinates with its wireline business; Qwest does not.

In these circumstances, it is inconceivable that the Verizon/MCI merger could be allowed to close without Verizon similarly being required to make a substantial divestiture of MCI assets, customers, and service operations in the Verizon territory on terms similar to the consent decree that the Department of Justice required of Qwest. Nothing has changed in a year that would change the competitive analysis here.

### B. Additional Conditions Would Be Necessary to Address Remaining Anticompetitive Effects in the Local Wholesale Market Even After Full Divestiture

Divestiture of overlapping in-region facilities, customers, and services alone would not be sufficient to address the competitive harms that would result from this merger. Even if MCI's

in-region operations were divested to a single CLEC, that CLEC would not have the size and scope to replace MCI as an overbuilder of the local network in the Verizon region, or as a reseller of Verizon special access. At least the existing MCI assets would be in independent hands. But the purchasing CLEC would be unlikely to have MCI's national traffic volumes and other strengths sufficient to replace MCI in expanding wholesale competition in the Verizon region. Furthermore, these problems would be even worse if the SBC-AT&T merger is approved. In that event, SBC is unlikely to continue AT&T's role as an aggressive access competitor in the Verizon region.

It follows that if the Commission is to approve Verizon's acquisition of MCI, it must go beyond requirements of divestiture, and affirmatively address the increased market power and enhanced anticompetitive incentives that Verizon would enjoy in the local wholesale market. These specific merger effects require specific merger-related solutions.

Verizon argues that access and other wholesale interconnection issues should be ignored in this proceeding, and instead addressed only in general rulemaking dockets. 118/ The Commission should ignore this suggestion, which disregards the specific and serious harm to wholesale competition in the Verizon region that would result from this merger. These effects would not arise in other parts of the country where AT&T and MCI would remain strong competitors under their new masters. To be direct, Verizon and SBC would generally continue to expand current AT&T and MCI wholesale activity in the Qwest region. But they will not do so in their own regions, or in each other's regions.

Qwest believes that any discussion of specific conditions is largely premature. Until the Applicants provide more information, a meaningful discussion of conditions that could even

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118/ *Public Interest Statement* at n. 33.

conceivably result in enhancing competition cannot be had. Preliminarily, however, and in addition to a full divestiture of overlapping facilities and customers, Qwest believes that any discussion of merger conditions must include at least four subjects. First, the Commission must take steps to ensure reasonable access to Verizon special access facilities. Qwest is aware, of course, that the Commission has commenced a general rulemaking to reconsider its special access pricing rules. But that is not a substitute for addressing the particular harmful effects that would be created in the Verizon service territory if this merger is approved, particularly in conjunction with SBC's acquisition of AT&T.

Second, the Commission must require Verizon to make stand-alone DSL available throughout its region on reasonable rates, terms and conditions. We have seen Verizon's recent announcements on this topic, but that is not a substitute for enforceable merger conditions across the Verizon service territory. In particular, announcements of a willingness to begin to provide stand-alone DSL are meaningless if the terms are not sufficient to allow competitive service offerings by non-Verizon VoIP providers and others.

Third, the Commission will need to develop merger conditions regarding local interconnection arrangements in the Verizon region, recognizing the critical role Verizon has played in leading the development of interconnection policies. This is a matter that will require more attention in the months ahead.

Fourth, the Commission should consider carefully conditions on how Verizon terminates VoIP traffic to its PSTN customers. We are aware that this issue is under review in the IP-Enabled Services Rulemaking and elsewhere. But however this issue may be resolved generically, the Commission will need to give special consideration to the increased market power that Verizon would enjoy in this area if it is allowed to capture MCI.

Again, this is just a preliminary discussion of conditions that would be required on top of full divestiture of overlapping MCI services, facilities and customers in the Verizon local service territory. Given the profound harmful effects that would flow from Verizon taking out one of its main rivals, the Commission would have to act aggressively to create a foundation for new competitors to replace MCI in both the wholesale and retail markets. Much more analysis will be required on this subject once Verizon supplements the record in this proceeding.

## CONCLUSION

The proposed merger of Verizon and MCI should be rejected. But if ultimately the Commission is able to approve this merger, that would be possible only with the substantial divestiture of MCI's in-region overlap, and appropriate conditions to address the loss in wholesale competition that would result. Anything less would result in serious anticompetitive harm and violate the public interest. In that event, the Commission would have no choice but to deny this merger.

Respectfully submitted,

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May 9, 2005

# VERIFICATION

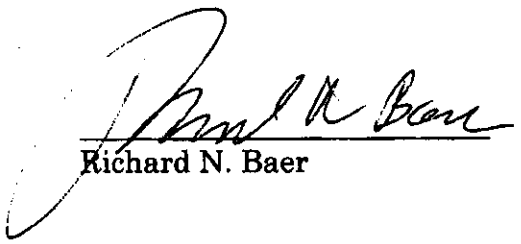
I, Richard N. Baer, hereby declare that I am the Executive Vice President, General Counsel and Secretary of Qwest Communications International Inc., and that I am authorized to make this Verification for and on behalf of the company. I have read the foregoing and the facts stated therein are true and correct to the best of my knowledge, information and belief.

Richard N. Baer

Dated: May 9, 2005

**VERIFICATION**

I, Richard N. Baer, hereby declare that I am the Executive Vice President, General Counsel and Secretary of Qwest Communications International Inc., and that I am authorized to make this Verification for and on behalf of the company. I have read the foregoing and the facts stated therein are true and correct to the best of my knowledge, information and belief.



Richard N. Baer

Dated: May 9, 2005